

## Message Text

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ACTION AF-06

INFO OCT-01 ARA-06 EUR-12 ISO-00 SP-02 AID-05 EB-07 NSC-05

CIEP-01 TRSE-00 SS-15 STR-04 OMB-01 CEA-01 CIAE-00

COME-00 FRB-03 INR-07 NSAE-00 USIA-06 XMB-02 OPIC-03

LAB-04 SIL-01 ITC-01 PA-01 PRS-01 AGR-05 INT-05 /105 W

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R 041514Z FEB 76

FM AMEMBASSY LUSAKA

TO SECSTATE WASHDC 2776

INFO AMEMBASSY LONDON

AMEMBASSY DAR ES SALAAM

AMEMBASSY PRETORIA

AMEMBASSY KINSHASA

AMEMBASSY BLANTYRE

AMEMBASSY GABORONE

AMEMBASSY NAIROBI

AMEMBASSY SANTIAGO

AMEMBASSY LIMA

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EO 11652: N/A

TAGS: EFIN, ZA

SUBJECT: 1976 BUDGET PRESENTATION

1. SUMMTJY: BEGIN UNCLASSIFIED. ZAMBIA'S DEPRESSED  
ECONOMIC SITUATION WAS STARKLY BUT ONLY PARTIALLY SKETCHED IN THE  
1976 BUDGET PRESENTED TO THE PARLIAMENT JANUARY 30. IT SHOWED  
NEGATIVE GROWTH THE PAST YEAR. NO REVENUES FROM COPPER OR  
OTHER MINERAL TAXES ARE ANTICIPATED FOR 1976. HERETOFORE  
THIS SOURCE SUPPLIED NEARLY 50 PERCENT OF TOTAL FISCAL REVENUES,  
OR WEPT OVER HALF A BILLION DOLLARS PZ COPPER'S BETTER YEARS.  
TO COPE WITH ITS ECONOMIC CRISIS ZAMBIA PROPOSES SUBSTANTIAL  
CUTBACKS IN CAPITAL AND CURRENT EXPENDITURES WHICH WILL FRUSTRATE  
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CERTAIN DEVELOPMENT PLANS; LEAST AFFECTED ARE HIGH PRIORITY

SECTORS OF EDUCATION, AGRICULTURE AND HEALTH. ADDITIONAL AND SIGNIFICANT SAVINGS SHOULD BE REALIZED AS THE GOVERNMENT MAKES A START ON DISMANTLING ITS COSTLY SUBSIDIES TO CONSUMER AND PRODUCERS, LONG POSTPONED FOR POLITICAL REASONS. IN THEIR PLACE, PRICE INCREASES WILL BE ALLOWED MANY BASIC COMMODITIES, WHICH SHOULD BE AN INCENTIVE TO AGRICULTURE. BUT THE 1976 BUDGET PRESENTATION POINTS UP ZAMBIA'S LIMITED POSSIBILITIES FOR RAISING DOMESTIC REVENUES TO A DEGREE WHICH WOULD COME ANYWHERE NEAR MAKING UP THE HUGE FISCAL DEFICIT.

2. THIS CURRENT BUDGET IS MORE A PEEK SHOW THAN A FULL REVELATION OF THE COUNTRY'S FINANCIAL NAKEDNESS RESULTING FROM THE COPPER SLUMP, RISING IMPORT COSTS, HIGHER GOVERNMENT OPERATING EXPENDITURES, AND TRANSPORT BOTTLENECKS. WHILE A BALANCE OF PAYMENTS DEFICIT OF \$280 MILLION WAS REPORTED FOR 1975, WITH A FIRST-EVER UNFAVORABLE TRADE BALANCE, NO BOP FIGURE WAS GIVEN FOR 1976, ALTHOUGH A FAIR ESTIMATE OF THE DEFICIT WOULD BE AROUND THREE QUARTERS OF A BILLION DOLLARS. THE MINISTER OF FINANCE QUANTIFIED EXTERNAL FINANCING NEEDS OF THE TWO MINING COMPANIES ALONE AT BETWEEN \$384-571 MILLION, DEPENDING ON TRANSPORT CONDITIONS.

3. IT APPEARS THE GOVERNMENT DELIBERATELY SOFT-PEDALED THE GRAVITY OF THE COUNTRY'S ECONOMIC AND FINANCIAL SITUATION SO AS TO DAMPEN POSSIBLE PUBLIC PROTEST. PRIVATELY THE GOVERNMENT HAS STATED ITS INTENTION TO SEEK DEFICIT COVER THROUGH EXTERNAL BORROWING. THE CENTRAL BANK GOVERNOR AND THE PERMANENT SECRETARY OF THE MINISTRY OF FINANCE HAVE ALREADY DEPARTED ZAMBIA TO COMB THE CAPITAL MARKETS OF WESTERN EUROPE AND NORTH AMERICA. IN ADDITION THE GRZ INTENDS TO PRESENT A STRONG CASE FOR DEVELOPMENT AND BALANCE OF PAYMENTS RELIEF IN THE RAW MATERIALS AND FINANCE COMMISSIONS AT THE CIEC MEETINGS STARTING THIS WEEKEND IN PARIS. END SUMMARY.

2. ECONOMIC PERFORMANCE IN 1975: BUDGET SPEECH EMPHASIZED GRAVITY OF 40 PERCENT DECLINE IN COPPER PRICES FROM AVERAGE OF \$2,068 PER TON IN 1974 TO \$1,231 IN 1975. BECAUSE OF FINANCIAL DIFFICULTIES AND UNAVAILABILITY OF SPARE PARTS, COPPER PRODUCTION FOR YEAR WAS 630,00 TONS, 14 PERCENT BELOW 1974 LEVEL. CLOSURE OF LOBITO PORT, WHICH IN 1974 HANDLED 55.1 PERCENT OF ZAMBIAN EXPORTS AND 44.6 PERCENT OF IMPORTS, CAUSED FURTHER STRAIN ON ZAMBIAN ECONOMY. AS A LIMITED OFFICIAL USE

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CONSEQUENCE,  
VOLUME OF TONNAGE EXPORTED DURING 1975 WAS  
17 PERCENT BELOW PREVIOUS YEAR WHILE VOLUME OF IMPORTS FELL  
9.4 PERCENT. EXPORT EARNINGS FELL FROM \$1.4 BILLION IN 1974 TO  
UNDER \$800 MILLION IN 1975 AND ZAMBIA EXPERIENCED FIRST TRADE  
DEFICIT IN ITS HISTORY. GDP IN CONSTANT (1965) PRICES FELL 3 PERCENT  
TO \$1,389 MILLION. IN CURRENT PRICES GDP DROPPED 20.4 PERCENT.  
CONSUMER PRICES FOR YEAR ROSE BY ABOUT 15 PERCENT. ALL SECTORS

SUFFERED FROM SHORTAGES OF IMPORTED INPUTS AND TRANSPORT BOTTLENECKS. APART FROM SUGAR INDUSTRY, AGRICULTURAL PRODUCTION WAS STAGNANT AND PRODUCTION IN MANUFACTURING SECTOR FELL ABOUT 2 PERCENT.

3. PUBLIC FINANCE IN 1975: ACTUAL GOVERNMENT EXPENDITURES IN 1975 OF \$947 MILLION FOR CURRENT EXPENDITURES AND \$353 MILLION FOR CAPITAL PROJECTS EXCEEDED REVENUES (INCLUDING BORROWING) BY \$380 MILLION. MAJOR SHORTFALL IN COPPER REVENUE - \$490 MILLION IN 1974 BUT ONLY \$94 MILLION IN 1975 - ACCOUNTED FOR BUDGET DEFICIT.

4. OUTLOOK FOR 1976. MINISTER PRESENTED CANDID BUT GENERAL APPRAISAL OF PROBLEMS FACING ZAMBIA IN COMING YEAR. RECOGNIZING LITTLE PROSPECT FOR IMPROVEMENT IN COPPER PRICES BEFORE LAST QUARTER OF 1976 AND THE PROBABILITY OF CONTINUED CLOSURE OF LOBITO DUE TO CIVIL WAR IN ANGOLA, MINISTER NOTES BOP SITUATION "WILL BE VERY CRITICAL" AND GRZ "REVENUES WILL BE AFFECTED VERY BADLY." IN EFFECT, MINISTER SAID, GRZ EXPECTS NO MINERAL TAX INCOME IN 1976. ONLY CLUE TO MINISTER'S ESTIMATE OF BOP OUTLOOK WAS HIS REMARK, MADE ALMOST IN PASSING, THAT ZAMBIA'S TWO MINING COMPANIES WILL REQUIRE ABOUT K246 MILLION (\$384 MILLION) OF EXTERNAL FINANCING IN 1976 "TO CONTINUE OPERATING SMOOTHLY." IF, HOWEVER, CONGESTION AT PORTS CONTINUES, THE REQUIREMENT WILL RISE TO K366 MILLION (\$571 MILLION). MINISTER GAVE NO INDICATION OF EXPECTED SOURCE OF THIS FINANCING.

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R 041624Z FEB 76

FM AMEMBASSY LUSAKA

TO SECSTATE WASHDC 2777

INFO AMEMBASSY LONDON

AMEMBASSY DAR ES SALAAM  
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5. REMEDIES: IN AN EFFORT TO REDUCE EFFECTIVE DEMAND, BUDGET CONCENTRATES ON FISCAL MEASURES. CURRENT EXPENDITURES ARE TO BE REDUCED BY \$104 MILLION, 11 PERCENT BELOW ACTUAL EXPENDITURES IN 1975, WITH EDUCATION, RURAL DEVELOPMENT & HEALTH RECEIVING LARGEST ALLOCATION. CAPITAL SPENDING BY GOVERNMENT WILL DECLINE 31 PERCENT TO UNDER \$245 MILLION. ONLY SPECIFIC REDUCTION IN EXPENDITURE INDICATED IN BUDGET WAS IN AREA OF SUBSIDIES TO CONSUMERS (\$57 MILLION IN 1975), PARASTATAL ORGANIZATIONS (\$12.5 MILLION), AND PRODUCERS (\$57 MILLION); THOUGH EXACT COSTS NOT GIVEN. COST OF THESE REDUCTIONS DRAMATICALLY BROUGHT HOME IN TERMS HIGHER NEW CONSUMER AND PRODUCER PRICES ANNOUNCED FEB 1. BUDGET INTRODUCES TAX CHANGES AIMED AT RAISING ADDITIONAL REVENUE OF \$69. MILLION. WHILE MUCH ATTENTION GIVEN TO INCREASES IN PERSONAL INCOME TAXES, THIS MEASURE EXPECTED TO PRODUCE ONLY LIMITED OFFICIAL USE

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\$3 MILLION. SELECTIVE EMPLOYMENT TAX ON SALARIES ON NON-ZAMBIANS INCREASED FROM 5 PERCENT TO 10 PERCENT TO ENCOURAGE COMPANIES TO ZAMBIANIZE WORK FORCE AND TO INCREASE REVENUE BY \$10 MILLION. SALES TAX EXTENDED TO ADDITIONAL GOODS, DUTIES ON AUTOMOBILES AND ALCOHOL RAISED, EXCISE TAXES ON BEER INCREASED BY ABOUT TEN CENTS A BOTTLE AND ON GASOLINE BY EIGHT CENTS A LITRE (TO \$1.74 PER U.S. GALLON). SUGAR PRICE RAISED MODESTLY. THESE MEASURES AIMED AT RAISING \$45 MILLION.

6. ON MONETARY SIDE, MINISTER PROPOSED INCREASE IN INTEREST RATES ON SAVINGS FROM 4 TO 5 PERCENT. TO DISCOURAGE BORROWING BANK RATE RAISED FROM 5 TO 6 PERCENT AND MAXIMUM LENDING RATE RAISED TO 11 PERCENT. AS INCENTIVE TO EXPATRIATE FARMERS, RESTRICTIONS ON BORROWING ELIMINATED. COMMERCIAL BANK'S LIQUIDITY RATIO RAISED TO FORCE LARGER DEPOSITS WITH CENTRAL BANK. NO ADDITIONAL EXCHANGE CONTROL MEASURES ANNOUNCED. END UNCLASSIFIED.

7. COMMENT: BEGIN LIMITED OFFICIAL USE. MOST GLARING DEFICIENCY OF BUDGET PRESENTATION IS NEAR TOTAL INADVERTENCE TO BOP OUTLOOK. WHILE MINISTER NOTED THAT 1975 BOP DEFICIT WOULD BE IN REGION OF \$281 MILLION, ALL SPECIFICS WERE OMITTED. WE

SUSPECT THAT DETERIORATION SIGNIFICANTLY WORSE THAN STATED SINCE DURING COURSE OF 1975 ZAMBIA ACCUMULATED SUBSTANTIAL FOREIGN EXCHANGE PAYMENTS ARREARAGES, PROBABLY IN RANGE OF \$200 MILLION. IF THESE ARREARAGES ARE TREATED AS INFLOWS ON CAPITAL ACCOUNT, TRUE BOP DEFICIT FOR 1975 WAS IN RANGE OF ONE HALF BILLION DOLLARS. SIMILARLY, BUDGET PRESENTATION TOTALLY IGNORES BOP OUTLOOK FOR 1976. ASSUMING NO IMPROVEMENT IN COPPER PRICES EXPORT EARNINGS IN 1976 WOULD BE IN RANGE OF \$750 MILLION. EVEN ASSUMING A 10 PERCENT REDUCTION IN THE VOLUME OF IMPORTS, BALANCE OF TRADE WOULD BE NEGATIVE IN RANGE OF \$100 MILLION. ADDITIONALLY, NET SERVICE AND TRANSFER PAYMENTS OF \$450 MILLION WOULD RESULT IN BOP DEFICIT ON CURRENT ACCOUNT OF \$550 MILLION.

8. ALTHOUGH NEED FOR PRICE INCREASES WAS IMPLICIT IN BUDGET AND SHOULD NOT HAVE COME AS SURPRISE, INCREASES ANNOUNCED FEB 1 LIKELY GENERATE STRONG PUBLIC REACTION AND MAY EXPLAIN IN PART DECLARATION ON JAN 28 OF STATE OF EMERGENCY. WHILE PRICE INCREASES LIKELY TO RECEIVE MOST ATTENTION, BUDGET ITSELF CONTAINS FEATURES WHICH WILL BE FELT INDIRECTLY. MINISTER GLOSSED OVER LIMITED OFFICIAL USE

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SPECIFICS OF REDUCTION IN PUBLIC SECTOR EXPENDITURES BUT IN VIEW OF TREND IN RECENT YEARS TOWARD INCREASE OF CURRENT EXPENDITURES, PRIMARILY SALARIES AND SERVICES, AS PERCENTAGE OF TOTAL EXPENDITURES, AN EXPENDITURE REDUCTION OF \$213 MILLION CAN BE ACHIEVED ONLY THROUGH SUBSTANTIAL REDUCTION IN PUBLIC SECTOR EMPLOYMENT.

9. IN LINE WITH RECENT GRZ POLICY, BUDGET PRESENTS SIGNIFICANT INCENTIVES FOR AGRICULTURAL SECTOR. INCREASED PRODUCER PRICES COME TOO LATE FOR CURRENT CROP YEAR AND EFFECTS IN TERMS OF INCREASED PRODUCTION WILL NOT SHOW UP UNTIL 1977. MOREOVER, SHIFT TO AGRICULTURE UNLIKELY TO EASE REVENUE OR BOP PROBLEMS OVER SHORT TERM.

10. CONTENT OF BUDGET PRESENTATION ITSELF SEEMS TO REFLECT GRZ DECISION NOT TO SPELL OUT TOO CLEARLY TO ZAMBIA PUBLIC ENORMITY OF ECONOMIC PROBLEMS FACING COUNTRY OR HARDSHIPS AND SACRIFICES EACH PERSON WILL HAVE TO BEAR AS GOVERNMENT TRIES TO COPE WITH SITUATION. GRZ APPARENTLY FEELS THAT BAD NEWS IN SMALLER DOSES THAN EXPECTED WILL BE MORE PALATABLE POLITICALLY THAN ALL AT ONCE. THUS, IMPLICATIONS OF REDUCED SUBSIDIES, ABSENCE OF REVENUE FROM COPPER INDUSTRY IN 1976, AND HUGE BOP DEFICITS WERE NOT SPECIFICALLY DEALT WITH IN BUDGET PRESENTATION. WITH SENIOR GRZ REPRESENTATIVES LEAVING FOR EUROPE AND NORTH AMERICA TO SEEK EXTERNAL FINANCING, WE INTEND REMAIN IN CLOSE TOUCH WITH KEY OFFICIALS TO LEARN HOW GRZ PROPOSES DEAL WITH SERIOUS PROBLEMS POSED BY THE BUDGET BUT FOR WHICH NO SPECIFIC SOLUTIONS OFFERED. WILKOWSKI

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## Message Attributes

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